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IN THE

Supreme Court of the United States

October Term, 1952

No. 698

CHARLES WELCH,

Petitioner,

against

ATLANTIC GULF AND WEST INDIES STEAMSHIP LINES,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF ATLANTIC GULF AND WEST INDIES STEAMSHIP LINES IN OPPOSITION

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Attorney for Respondent Atlantic Gulf and West Indies Steamship Lines.

FREDERICK F. GREENMAN
DANIEL M. SANDOMIRE
ROBERT H. HAINES
Of Counsel

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Opinions Below

The opinion of the District Court of the United States for the Eastern District of New York is reported at 101 F. Supp. 257. The opinion of the Court of Appeals for the Second Circuit is reported at 200 F. 2d 199.

Jurisdiction

The judgment of the Court of Appeals was entered on December 19, 1952 (R. 90),* and the order denying the

*The record herein is in three parts: the Appendix to petitioner's brief in the court below, the Appendix to respondent's brief below, and the proceedings in the Court of Appeals. References herein to petitioner's Appendix are prefixed by "P" followed by the page number; references to respondent's Appendix are prefixed by "D"; and references to the third portion of the printed record are prefixed by "R".

petition for rehearing was entered on January 6, 1953 (R. 94). The petition for a writ of certiorari was filed on April 4, 1953. This Court's jurisdiction is invoked by petitioner under Section 1254 of the United States Code, Judiciary and Judicial Procedure.

Judgment Sought To Be Reviewed

The judgment below was entered upon a brief PER CURIAM opinion of the Court of Appeals (Swan, *Chief Judge,* Chase and Clark, *Circuit Judges*). The opinion was as follows:

> "Action by a holder of non-cumulative preferred stock to obtain a decree for payment of dividend arrears. From an adverse summary judgment, the plaintiff appeals.
>
> * * * * *
>
> "PER CURIAM: Judgment is affirmed on the opinion below, 101 F. Supp. 257. The appellant's effort to distinguish *Guttmann* v. *Illinois Central R. Co.,* 2 Cir., 189 F. 2d 927, cert. den. 342 U. S. 867, cannot prevail. The sentence upon which counsel relies for the attempted distinction is a restriction upon the payment of dividends on the common stock; it does not impose an obligation to pay passed dividends on the non-cumulative preferred. That this is the correct interpretation is confirmed by the provision giving the corporation the option to purchase preferred stock at par, as well as by the provision governing liquidation and dissolution of the corporation."

Questions Presented

Petitioner in support of his application for certiorari would make it appear to this Court

(1) that the courts below, denying the right of holders of respondent's non-cumulative preferred stock to recover alleged dividend arrears, incorrectly interpreted the provisions of respondent's charter defining the rights of such preferred stockholders,—in particular, that they incorrectly interpreted one sentence of that charter to which the Court of Appeals made direct reference in its brief *per curiam* opinion; and

(2) that the Court of Appeals in so holding incorrectly applied its decision in *Guttmann* v. *Illinois Central R. Co.*, 189 F. 2d 927 (CA 2, 1951), cert. den. 342 U. S. 867 (1952), where it had previously considered the rights of non-cumulative preferred stockholders to back dividends.

There Is No Merit In the Petition

Admittedly, no federal question is involved in this case. Moreover, there is no assertion that the decision below conflicts with that of any other circuit. Nor does petitioner contend that the decision below conflicts with any decision of this Court.

Petitioner asserts two reasons for granting the writ: (1) that "the question here presented is important to the business community" because "many large corporations in this country have non-cumulative preferred stock outstanding" (petition, p. 7); and (2) that the decision below was incorrect in view of the particular terms of the corporate charter here concerned (petition, p. 8 *et. seq.*).

These two "reasons", as petitioner advances them, are substantially contradictory. Even if there are many non-cumulative preferred stock issues in existence, as petitioner

suggests, the point which he seeks to present here is a peculiarly narrow one. His claim to back dividends is rested upon one particular sentence of respondent's charter. His argument requires him to assert that "the preferred stock herein is certainly not the conventional non-cumulative preferred stock" but "a hybrid" (petition, pp. 10, 13). Thus, it is the petitioner who asserts that his case is unique; and this assertion is essential to his position.

With respect to the views of the business community on the subject of the payment of back dividends on non-cumulative preferred stock, this Court has expressed its opinion. Mr. Justice Holmes in *Wabash Ry. Co.* v. *Barclay,* 280 U. S. 197, 203 (1930), summarized the views of the business community on this subject as follows:

> "We believe that it has been the common understanding of lawyers and business men that in the case of non-cumulative stock entitled only to a dividend if declared out of annual profits, if those profits are justifiably applied by the directors to capital improvements and no dividend is declared within the year, the claim for that year is gone and cannot be asserted at a later date."

This statement of "common understanding" is fully confirmed by Professor A. A. Berle, the principal advocate of greater rights for non-cumulative preferred stockholders, as the Court of Appeals for the Second Circuit noted in its opinion in *Guttmann* v. *Illinois Central R. Co.,* 189 F. 2d 927 (1951), cert. den. 342 U. S. 867 (1952):

> "Berle, a most brilliant legal commentator on corporate finance, who may be credited with the authorship of plaintiff's basic contention, admitted that 'popular interpretation,' including that of 'in-

> vestors and businessmen,' holds 'non-cumulative' to mean 'that dividends on non-cumulative preferred stock, once passed or omitted, are "dead"; can never be made up.' See Berle, Non-Cumulative Preferred Stock, 23 Columbia Law Review (1923) 358, 364-5" (189 F. 2d, at 930n).

The Maine courts as far back as 1887 arrived at similar views. *Belfast & Moosehead Lake R. Co.* v. *Belfast*, 77 Me. 445, 1 Atl. 362 (1885), and *Hazeltine* v. *Belfast & Moosehead Lake R. Co.*, 79 Me. 411, 10 Atl. 328 (1887). Incidentally, these are the only cases in Maine which deal with non-cumulative preferred stock. The following statements by the Maine Supreme Judicial Court in these two opinions concur with the views of the business community on the subject:

> "It was not intended in the present instance to guarantee a dividend. If a dividend is prevented in any one year by a deficit of earnings, it cannot be made up from the earnings of succeeding years" (77 Me. at 452, 1 Atl. at 365).
>
> "Another thing, before spoken of, which favors the complainants is that by our former opinion their dividends are held to be non-cumulative, and if lost now are forever lost" (79 Me. at 420, 10 Atl. at 331-2).

Petitioner's second reason for review in this Court is his attack upon the decision below, raising the questions on the merits which we have set forth above (*supra*, pp. 2-3). It is our position with respect to these questions that the court below correctly interpreted the corporate charter concerned, and that it correctly determined the law of the corporate domicile—the State of Maine—which, it is agreed, is applicable. Our position with respect to these questions is

fully set out in the short brief which we submitted to the Court of Appeals; accordingly, we annex a copy of that brief hereto. The decision below, we submit, is correct; there is no reason for granting the writ of certiorari.

CONCLUSION

No question of federal law, and no inconsistency of decision either with this Court, with other circuits, with the law of Maine, or with the law of New York is presented; nor is any question presented of such wide interest as would warrant the granting of a writ of certiorari.

Respectfully submitted,

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United States Court of Appeals

FOR THE SECOND CIRCUIT

CHARLES WELCH,
Plaintiff-Appellant,

against

ATLANTIC GULF AND WEST INDIES STEAMSHIP LINES,
Defendant-Appellee.

BRIEF FOR DEFENDANT-APPELLEE

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United States Court of Appeals

FOR THE SECOND CIRCUIT

CHARLES WELCH,
Plaintiff-Appellant,

against

ATLANTIC GULF AND WEST INDIES STEAMSHIP LINES,
Defendant-Appellee.

BRIEF FOR DEFENDANT-APPELLEE

This is an appeal by plaintiff from a judgment of the District Court (Galston, *J.*) granting defendant's motion for summary judgment under Rule 56(b) F. R. C. P. and dismissing the complaint. Judge Galston's opinion is reported at 101 F. Supp. 257, and is set forth in the printed Appendix to plaintiff-appellant's brief (pp. 187-194a).

The record below consisted of affidavits submitted by both parties, exhibits thereto, and depositions of each party taken by the opposing party. The entire record has been filed in this Court. Plaintiff-appellant has printed in his Appendix the pleadings, the order, judgment and opinion of the District Court, and the text of all affidavits submitted below, omitting the exhibits. Defendant-appellee's Appendix contains two of the exhibits and plaintiff's deposition. References in this brief to such printed portions of the record are prefixed by the letter "P" to refer to pages of plaintiff-appellant's Appendix, and by the letter "D" to refer to pages of defendant-appellee's Appendix.

Preliminary Statement

The action is brought by a holder of non-cumulative preferred stock of defendant corporation seeking recovery of alleged dividend arrears. The decision below dismissing the complaint was placed squarely on the authority of *Guttmann* v. *Illinois Central R. Co.*, 189 F. 2d 927 (CA 2, 1951), cert. den. 342 U. S. 867 (1952), and upon the terms of the corporate charter defining the rights of the preferred stockholders. The law of Maine—the state of incorporation—is in full accord, as we shall show, with the general rule followed in the *Guttmann* case.

We set forth here in full the provisions of defendant's certificate of incorporation defining the rights of preferred stockholders (P44-5):

> "The holders of the preferred stock shall be entitled to non-cumulative dividends, payable from the surplus or net profits of the corporation, at the rate of but not exceeding five per centum (5%) per annum for each and every fiscal year, when and as determined and declared by the Board of Directors, in preference and priority to any payment for such fiscal year of any dividend on the common stock.
>
> "If after earning, declaring and appropriating for the preferred stock a dividend of five percent. (5%) for any fiscal year there shall remain any surplus or undivided net profits for such fiscal year, the Board of Directors out of such surplus or undivided net profits may declare and pay dividends for such fiscal year upon the common stock. But no dividends shall in any fiscal year be paid upon the common stock out of any surplus or net profits of any previous fiscal year for which the full dividends shall not have been paid on the preferred stock. The preferred stock or any portion thereof may, from time to time, be purchased by the corporation, at its option,

upon the payment in cash of one hundred dollars ($100) per share to the holder or holders of the preferred stock so to be purchased, ten days' notice of such proposed purchase having been given. Preferred stock so purchased shall be held in the Treasury of the corporation and no dividend shall be paid thereon until and unless the Board of Directors by the vote of a majority shall authorize the sale of the same and the payments of dividends thereon; it being the intention that such purchase shall not be construed as a reduction of the capital stock of this corporation.

"In the event of any liquidation, dissolution or winding-up, whether voluntary or involuntary, of the corporation, the holders of the preferred stock shall be entitled to be paid in full the par value of their shares before any amount shall be paid to the holders of common stock, and after such payment to the holders of the preferred stock of its par value the remaining assets and funds shall be divided and paid to the holders of the common stock."

Appellant's quotation (brief, p. 5) from this portion of the charter omits the provisions above relating to redemption of the preferred stock and its rights on dissolution and liquidation,—provisions which we regard as having significance here. The full provisions above are set forth as well on the face of the preferred stock certificates (P173-5). There is no controversy with respect to their terms.

We also set forth at this point the dividend record of the defendant corporation since its organization,* as follows:

*The dividend payments for the years 1909 through 1950 appear on the record herein in tabular form in the original motion papers (D3; see, also, P50-52). The dividends for the year 1951 were in part paid after the summary judgment motion had been made; evidence with respect thereto appears in the subsequent affidavits (P177, 180).

	Dividends Paid Per Share	
	Preferred Stock	Common Stock
1909	$—	$—
1910	—	—
1911	—	—
1912	—	—
1913	—	—
1914	—	—
1915	—	—
1916	5	5
1917	5	11
1918	5	10
1919	5	10
1920	5	10
1921	—	—
1922	—	—
1923	—	—
1924	—	—
1925	—	—
1926	2	—
1927	5	—
1928	—	—
1929	5	3
1930	5	—
1931	—	—
1932	—	—
1933	—	—
1934	—	—
1935	—	—
1936	3	—
1937	—	—
1938	—	—
1939	—	—
1940	—	—
1941	5	3
1942	5	3
1943	5	3

	Dividends Paid Per Share	
	Preferred Stock	Common Stock
1944	5	3
1945	5	3
1946	5	3
1947	5	3
1948	5	1
1949	5	—
1950	5	1
1951	5	2

It may thus be seen that during each of the past eleven years, as well as in a number of earlier years, the full dividend of $5 per share has been paid on the preferred shares outstanding. This action, as a result, is confined to the question of dividends for years in which the full dividend was not paid (1940 and earlier) and to the right of the preferred stockholders to seek such back dividends now. As Judge Galston stated below, "There is no allegation of fraud on the part of the directors of those years, or of bad business judgment" (101 F. Supp. at 261; P194). (Such a charge now would, of course, be barred by the statute of limitations.*)

The right to back dividends depends entirely on the charter provisions and their interpretation. Judge Galston's decision is so confined (P191-194a; 101 F. Supp. at 260-1).

*The New York statute of limitations governs. *Guaranty Trust Co.* v. *York*, 326 U. S. 99 (1945). The ten-year period of limitations (C. P. A. Sec. 53) would apply to any such claim; operation of the statute is not postponed even where a plaintiff injects allegations of fraud to bolster his claim. *Lever* v. *Guaranty Trust Co.*, 262 App. Div. 1044, 1045 (2d Dept. 1941), aff'd. mem. 289 N. Y. 615 (1942); *Hastings* v. *H. M. Byllesby & Co.*, 293 N. Y. 404, 411-2 (1944); *Pollack* v. *Warner Bros. Pictures, Inc.*, 266 App. Div. 118, 120 (1st Dept. 1943); *Laird* v. *United Shipyards, Inc.*, 163 F. 2d 12 (CA 2, 1947) cert. den. 332 U. S. 842 (1947); cf. also, *Austrian* v. *Williams*, CA 2, Aug. 15, 1952, p. 1667 (not yet reported).

Other matters set forth in the record are peripheral in their nature, supplying background and detail, and also dealing with plaintiff's charge that the present directors act with improper motives when they decline to accept plaintiff's interpretation of the charter and refuse to vote the back dividends on the preferred stock which plaintiff here claims. This last obviously can have no bearing on the question of interpretation of the charter upon which the case rests.

STATEMENT OF FACTS

Plaintiff's action was commenced on November 8, 1950. It is significant that the complaint was filed prior to the decision of this Court in *Guttman* v. *Illinois Central R. Co., supra.* It was evidently framed in reliance upon *Collins v. Portland El. Power Co.*, 12 F. 2d 671 (CA 9, 1926). But the authority of that case was rejected in the *Guttman* decision; this Court noted that the *Collins* case had been cited to the Supreme Court in *Wabash Ry. Co.* v. *Barclay,* 280 U. S. 197 (1930), and that it was "at odds with the rationale of the Wabash decision" (189 F. 2d, at 930).

Plaintiff seeks judgment, as set forth in the prayer of his complaint (P14), declaring that "there were sufficient earnings or surplus in prior years to pay the sum of $6,400,000.00 now in arrears on the Agwi preferred stock and that said sum is presently due and payable to the holders of such stock"; decreeing that such alleged dividend arrearages of $6,400,000 be paid forthwith; and enjoining the declaration of dividends on the common stock until such alleged arrearages on the preferred stock are paid in full.

Plaintiff, a resident of New York and an officer of a stock brokerage concern, according to his testimony herein

acquired his shares of preferred stock in May 1949 when 200 of such shares were registered in his name (D13). A rumor that the stock, then selling at 85, would soon be redeemed at par caused him to act (D31-4, 55); he had no other information; his sole interest was in "a possible profit of 15 points" (D44), a hope which has since been fully realized (see *infra*, p. 8n); whether the stock was cumulative or non-cumulative, he testified, "I didn't know and I didn't care" (D44). The shares were acquired, he says, in a transaction in which Joseph Schwebel (brother of his attorney herein) bought and paid for 200 shares, had them registered in plaintiff's name, and agreed orally that plaintiff was to receive one-half the anticipated market profit on 100 shares (P104-5, D30-31, 37).

Defendant was organized on November 25, 1908 under the laws of the State of Maine. Through its subsidiaries it has engaged in the operation of steamship lines. The corporation was formed pursuant to a plan of reorganization of a predecessor company which had defaulted on a $60,000,000 bond issue, and the plan provided for the distribution to the old bondholders of the bonds, preferred stock and common stock of the new company (P41; the plan, not printed, is Exhibit 1 annexed to the affidavit of A. G. Plett, Sept. 6, 1951). The new company's securities were widely held; its stock (preferred and common) was listed on the New York Stock Exchange in 1916 and later registered under the Securities Exchange Act of 1934; its stockholders were kept regularly advised of its business and affairs through the usual series of annual reports as well as information filed with the Stock Exchange and the S. E. C. (P52-3).

Defendant's bonds have been reacquired and redeemed (P42-3). Its preferred stock, of which 149,964 shares were originally issued, has been reaquired and retired from time to time beginning as early as 1915 with the result that there were only 25,812 shares outstanding at the time this case was submitted to the District Court (P42-4, 144, 152-3).* Common stock remains outstanding to the extent of 150,000 shares; the original par value of $100 per share, however, has been reduced from time to time to the present par value of $1.00 per share (P44).

Plaintiff's claim to relief.

The pleadings have already been well summarized in the District Court opinion (101 F. Supp. at 258--9; P188-190). The allegations of the complaint which present the issue to be decided here are found in two paragraphs. Paragraph Twentieth states:

> "The Agwi preferred dividends are designated as non-cumulative but no common dividends may in

*Since the decision of the District Court herein, the 24,712 preferred shares which then remained outstanding were redeemed by the corporation by the exercise of the option granted to it in the charter to purchase such shares at $100 per share on 10 days' notice. Upon such notice, all outstanding shares were redeemed and reacquired on December 17, 1951, and the entire redemption price irrevocably deposited by the corporation with Manufacturers Trust Company for payment to the preferred stockholders upon surrender of their respective stock certificates. Upon action taken at the annual meeting of stockholders held on April 22, 1952, all preferred shares were retired and the corporate charter amended accordingly. Since redemption on December 17, 1951, all preferred stock certificates have been surrendered and the redemption price paid to the holders thereof, with the exception of certificates for 335 shares; 200 of these are registered in the name of plaintiff, 100 in the name of Bertha W. Lann who is represented by plaintiff's attorney, and 35 in various other names.

> any year be paid out of surplus or net profits of any previous year for which full preferred dividends have not been paid; the amount of surplus that cannot under this provision be paid in dividends on the common stock while any preferred shares are outstanding, is calculated at approximately $6,400,-000.00 as of July 31, 1949" (P8-9).

Paragraph Twenty-first declares that "the sum of $6,-400,000 [is] rightfully the property of the Agwi preferred stockholders" (P9). The first part of paragraph Twentieth refers to the provisions of the charter; the latter part states the amount of the surplus subject to the restrictive provision of the charter, and this calculation is not controverted upon these proceedings. However, the succeeding allegation which claims ownership of the restricted portion of the surplus for the preferred stockholders is a conclusion of law which raises the question to be determined here.

The remainder of the complaint is devoted to plaintiff's charges concerning the motives of the present directors in respect of plaintiff's claimed dividend arrearages. In December 1948, a group of persons headed by Jerome A. Newman acquired approximately one-half of the outstanding common stock of defendant and thereby came into control of the corporation; the details of this transaction are set forth at considerable length in the complaint (P5-8). This group (called the Graham-Newman Group by plaintiff) "pursuant to a common plan or scheme" seek "to eliminate the preferred stock by devious means in order to declare unto themselves a dividend on their common stock holdings including the sum of $6,400,000 rightfully the property of the Agwi preferred stockholders" (P9); and to such end, the complaint continues, these persons have

caused the corporation to sell certain properties so that such dividend might be paid with the proceeds (P9), and have caused the corporation to make an exchange offer to the preferred stockholders and to retire the preferred shares surrendered thereunder (P9-10). Appellant's brief in this Court (p. 12) again refers to these charges. But he fails at any point to mention, in the case of the sales that he criticizes, that the properties sold were those of defendant's coastwise service which had been discontinued in 1947 and liquidation of its property then begun (well before the appearance of the Graham-Newman Group) (P94-5, 148-9), and the properties of defendant's Puerto Rico Line which in the year 1948 had suffered a loss from operations of over $700,000 (P94), the continuance of which was avoided by its sale (P94-5, 62-8). In referring to the preferred stock exchange offer and the retirement of preferred shares, appellant makes no mention of the fact that the corporation had been reacquiring and retiring preferred shares for many years (P43-144), nor of the fact that the 1949 exchange offer was presented to the stockholders through a full Prospectus filed with the S. E. C. under the Securities Act of 1933 which set forth the relevant facts in most minute detail (P54-5). (The Prospectus, not printed, is annexed as Exhibit 6 to the reply affidavit of A. G. Plett, Oct. 26, 1951.)

A considerable portion of the affidavits and other materials submitted by defendant below was devoted to these charges so that the record might not be barren in respect of such allegations of impropriety and misconduct. But these matters do not in any sense bear upon the issue which is determinative of the case. Either the preferred stockholders had a right to dividend arrears prior to the payment of dividends on the common stock, or they did not.

Either the directors were required to pay such back dividends on the preferred before paying common dividends, or they were not. The question is one of law, not motives. The terms of the charter must determine the issue.

In his complaint and in his argument before the District Court, plaintiff asserted that the preferred stockholders were entitled to the entire sum of $6,400,000. This is the portion of the surplus account subject to the restriction imposed by the charter on the payment of common dividends. Its computation is fully set forth in the record (D3). It consists of the surplus of the corporation for each year in respect of which the full preferred dividend was not paid. Such surplus for any year includes the earnings of that year and also other items, not earnings, which increase the surplus account. An instance is the 1931 surplus of $3,908,000 which consists, to the extent of $3,792,000, in surplus resulting from the reduction of the par value of the common stock (P77-8, D3). Other instances of "book" figures which are included in the restricted portion of the surplus account appear in the record (P76, 79-80). The complaint sought payment of the entire $6,400,000, asserting that the restricted portion of the surplus is "rightfully the property of the preferred stockholders", and stressing the fact that the corporation now has cash in such amount.

The absurdity of such claim is demonstrated by the fact that in the forty-three years of the corporation's existence to December 31, 1951, an aggregate of $100 per share has been paid in preferred dividends, and, at the full preferred dividend rate of $5 a year, dividends omitted amount in the aggregate to no more than $115 a share (see *supra*, pp. 4-5). Yet plaintiff sought distribution of $6,400,000 to the preferred stockholders which would have meant a dividend of $248

a share upon each of the 25,812 shares outstanding at the time the case was argued below (P153). No torturing of the charter provisions under the guise of "interpretation" could possibly lead to this result. Recognition of this has evidently caused plaintiff to shift his argument in this Court. He now appears to assert that unpaid dividends on the preferred stock were cumulative to the extent earned, and to restrict his claim to the omitted dividends for the years in which there were sufficient earnings. The amount so claimed is necessarily much smaller than $6,400,000. But plaintiff still uses the restrictive provision of the charter as the foundation of the "interpretation" which he seeks to make of that document.

SUMMARY OF ARGUMENT

1. Under the terms and provisions of defendant's charter, the preferred shareholders' right to dividends is explicitly non-cumulative. The charter language leaves no room for "interpretation" to alter its plain terms.

2. Dividends on non-cumulative preferred stock, once passed by the directors in the exercise of their discretion, are forever lost; no right survives to have those dividends declared subsequently, and the directors thereafter have no discretion whatever to declare those dividends. The law of Maine conforms fully to the general rule on this point set forth in *Wabash Ry. Co.* v. *Barclay*, 280 U. S. 197 (1930), and in *Guttmann* v. *Illinois Central R. Co.*, 189 F. 2d 927 (CA 2, 1951), cert. den. 342 U. S. 867 (1952).

3. There is no genuine issue of fact presented for trial; summary judgment was properly granted.

ARGUMENT

I

THE PREFERRED SHAREHOLDERS' RIGHT TO DIVIDENDS IS EXPLICITLY NON-CUMULATIVE UNDER DEFENDANT'S CHARTER

Any right of preferred stockholders to back dividends must be founded on the corporate charter. The charter provisions here (*supra*, pp. 2-3), with the exception of one sentence, parallel directly those that were considered in *Wabash Ry. Co.* v. *Barclay* and *Guttman* v. *Illinois Central R. Co.*, the controlling decisions on the subject (see *infra*, pp. 20-24). The single sentence which departs from the provisions considered in *Wabash* and *Illinois Central* is the sentence upon which plaintiff rests his entire case. It is as follows:

> "But no dividends shall in any fiscal year be paid upon the common stock out of any surplus or net profits of any previous fiscal year for which the full dividends shall not have been paid on the preferred stock."

This provision is a restriction on the payment of common dividends. It is clearly negative in its terms. Yet plaintiff attempts to turn it into an affirmative obligation to pay back dividends on the preferred. His argument requires a painful torturing of the language of the sentence. It also requires that the sentence be torn from its context and that all other provisions concerning the preferred stock be ignored. The charter expressly provides that "the holders of the preferred stock shall be entitled to *non-cumulative*

dividends" (italics added). In addition, it provides that "the preferred stock or any portion thereof may, from time to time, be purchased by the corporation, at its option, upon the payment in cash of one hundred dollars ($100) per share to the holder or holders of the preferred stock so to be purchased, ten days' notice of such proposed purchase having been given". Moreover, in the event of liquidation, dissolution or winding-up, the preferred stockholders receive the par value of their shares in priority to any payments on the common, and all remaining assets and funds by express provision go to the common shareholders. Redemption at par and dissolution distribution at par are completely inconsistent with the claim to dividend accumulations.

The restrictive provision, read without distortion and in accordance with its clear language, is entirely consistent with the other provisions governing the rights of the two classes of stock. It is purely and simply a restriction upon common dividends, and no more. Its object is clear. The preferred dividends are non-cumulative and are payable each year only "when and as determined and declared by the Board of Directors". The authors of the charter thus contemplated that there would be years in which profits would not be distributed upon the preferred stock. The dividend once passed is lost forever. The profits of that year may not be paid out to the preferred holders in the future. Under the restrictive provision, neither may those profits be paid out to the common stockholders while the preferred is outstanding. A result of this is that the preferred stockholders gain an incidental advantage from the freezing of such earnings; they are retained by the corporation and serve as a buffer, an additional protection for the outstanding

preferred shares. Plaintiff has himself tacitly conceded this when, in his complaint, he alleged that "the amount of surplus that cannot under this provision be paid in dividends on common stock *while any preferred shares are outstanding,* is calculated at approximately $6,400,000.00 as of July 31, 1949" (P8-9) (italics added). In its aspect as a protection for the preferred, the provision has the same effect as other types of restriction upon common dividends for the benefit of preferred shareholders. An example appears here in the case of the preferred stock of defendant's subsidiary, New York and Cuba Mail Steamship Company; the Cuba Mail charter provides that no dividend or distribution may be paid on the common unless the company shall retain a net worth at least three and one-half times the par value of the outstanding preferred shares (Prospectus, p. 29, not printed; Exhibit 6 annexed to reply affidavit of A. G. Plett, Oct. 26, 1951). The portion of the Cuba Mail surplus thus restricted as at July 31, 1949 was over $9,000,000, and the unrestricted portion of the surplus $646,000 (*ibid.*). But a restriction on surplus in any case, whether calculated upon prior earnings or by some other formula, is a restriction, and no more; it cannot, without more, create an obligation to pay the restricted amount to the preferred shareholders.

Plaintiff argues that the restriction on common dividends necessarily implies that the restricted portion of the surplus must be paid to the preferred holders. This is a complete *non sequitur*. Pursuing his original premise, plaintiff claimed the entire amount restricted—$6,400,000. The fantastic consequence of that claim has already been noted (*supra,* p. 11). Plaintiff now appears to be more moderate. His brief in this Court suggests that here he seeks only the omitted dividends to the extent that they were earned. But

he still depends on "interpretation" of the charter terms which involves a complete rewriting of that document. The authors of the charter provided for a restriction upon certain profits or surplus when preferred dividends were omitted. Had they intended that such dividends accumulate for subsequent payment on the preferred stock, it must be assumed that they would have said so. Provisions for such purpose had long been known. It would have been simple to say "cumulative if earned". Certainly, it is not to be assumed that the incorporators here were intent upon concealing their meaning at this point, as they must have been if we accept any of plaintiff's conclusions. On the contrary, the incorporators expressly anticipated that preferred dividends would be omitted even though at times there would be current earnings or surplus. They prohibited the use of such earnings or surplus for future dividends on the common stock. As to the preferred, they said without the slightest ambiguity that its dividends were to be non-cumulative. This, we submit, is the clear, explicit and unambiguous reading of the charter.

It is in realization, perhaps, of the lack of support to be found in any of the provisions of this portion of the charter—where definition of the preferred shareholders' rights should properly be found—that plaintiff turns to another part of the document and seeks support from the language of paragraph 12 (Brief, pp. 10-11). Paragraph 12 permits the directors to set aside reserves for various corporate purposes including "the equalizing of dividends" (P145-6, D5). But this does not advance plaintiff's argument. What plaintiff seeks here is not the use of earnings of an earlier and more profitable period to pay a current dividend which would otherwise be omitted, and thus obtain

equalization in dividend payments. The result plaintiff seeks is just reverse. The full $5 dividend has been paid regularly for the past eleven years. Plaintiff seeks to use earnings from earlier years when no preferred dividend was paid for payment now to the preferred stockholders in addition to their full current dividend. His result would not be "the equalizing of dividends" in any sense of the term.

Paragraph 12 of the charter has no relevance here. It is included in that portion of the charter which deals with the powers of the directors. Among other things, they are permitted to set up reserves for various corporate purposes, and among these purposes is the equalizing of dividends. This is a standard provision found in many corporate charters. Creation of reserves for future contingencies is by express terms placed within the directors' discretion. In permitting reserves for dividend equalization, it has bearing in the case of common dividends and specifically permits the directors to adopt a policy of dividends at a regular rate on the common stock without regard to fluctuations in earnings from year to year. It scarcely appears applicable in the case of non-cumulative preferred stock, and obviously no such reserve was ever created (P155-6). However, plaintiff here is not seeking any equalizing of dividends; he sues to recover alleged arrearages and to compel their payment in addition to the full current dividend. The fact that the directors had power to create reserves for future use to equalize dividends is most remote from the issue. Such power, in no event, can turn an expressly non-cumulative stock into one with cumulative dividend rights.

Plaintiff's strenuous efforts at "interpretation" must also run afoul of the dividend history of this corporation which we have set forth above (pp. 4-5). The preferred

stock and common stock of defendant corporation have been outstanding in the hands of the public since its incorporation in 1908. Both issues have been listed on the New York Stock Exchange since 1916 (P53). All shares, preferred and common, had full voting rights share for share (P4, 44). Holders of substantial amounts of preferred stock sat on the board of directors at all times up to 1949 (P49-50). At no time during this entire period has more than the $5 dividend been paid on the preferred in any year. Dividends on the common stock were paid, with three exceptions, in every year in which the preferred received the full $5 dividend. Plaintiff here claims that the preferred stock is entitled to "cumulative-if-earned" back dividends, and he seeks to enjoin the payment of common dividends until the claimed arrearages on the preferred are paid (P14). But if the preferred is entitled to such back dividends now, it was entitled to them on each occasion in the past when a common dividend was paid. It will not do to say, as does plaintiff in his brief (p. 11), that the charter called for "suspension to such time when the company has liquid funds". The argument refutes itself. Either the preferred shareholders here were entitled to back dividends in preference and priority to common dividends, or they had no such right at all. "Liquid funds", funds available for the payment of dividends to stockholders, were necessarily in the possession of the corporation on each occasion when it paid dividends on the common. Such funds were nevertheless paid out as dividends on the common stock; they were not used to pay back dividends on the preferred. The total dividends paid on the common during the 1916-1920 period amounted to more than $6,800,000; over $500,000 was paid on the common for 1929; and

$3,450,000 was paid as common dividends between 1941 and 1950 when this action was begun (D3). As we have already mentioned, the directors who declared these dividends up to 1949 included holders of substantial amounts of preferred stock. Nevertheless, at no time was a dividend of more than $5 paid on the preferred in any year, nor has any such additional dividend been claimed until this lawsuit. This is the first time that a claim is advanced that the preferred stock, specifically designated non-cumulative, is nevertheless cumulative. It is significant that this claim is advanced by one who acquired his interest only in 1949. The clear language of the charter had been accepted for over forty years as meaning just what it says by the corporation and by its stockholders, both common and preferred.

For further support for his "interpretation" plaintiff turns to four decisions which he cites in his brief (p. 10).* But in no instance does he cite a decision in which preferred stock specifically designated "non-cumulative" in the corporate charter was held to have cumulative dividend rights in any sense; nor does the student note from the Michigan Law Review which plaintiff quotes (brief, p. 10), despite its statement to the contrary, cite any such decision. We venture to suggest that there is no such case. What was involved in the cases that plaintiff and the law review editors present was charter language of considerable ambiguity which the courts were required to construe.

The charter here, we submit, is clear; it must be taken to mean just what it says. This is the contract between the parties. Judge Frank's observation in the *Guttmann* case

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**Garrett* v. *Edge Moore Iron Co.*, 22 Del. Ch. 142, 194 Atl. 15 (1937); *In re Louisville Gas & El. Co.*, 77 F. Supp. 176 (D. Del. 1948); *Warburton* v. *John Wanamaker*, 329 Pa. 5, 196 Atl. 506 (1938); *Foster* v. *Coles*, 22 T. L. R. (Ch.) 555 (1906).

is equally applicable here: "Nothing in the wording of that contract would suggest to the ordinary wayfaring person the existence of a contingent or inchoate right to arrears of dividends" (189 F. 2d, at 930). Here, indeed, not merely wayfarers but those directly concerned have for many years accepted the charter terms with no attempt at the extravagant interpolation that plaintiff now advances. "The holders of the preferred stock shall be entitled to non-cumulative dividends, * * *" This is the plain and unequivocal language of the charter. Plaintiff may not call upon the courts now to rewrite the contract.

II

DIVIDENDS ON NON-CUMULATIVE PREFERRED STOCK, ONCE PASSED BY THE DIRECTORS IN THE EXERCISE OF THEIR DISCRETION, ARE FOREVER LOST; NO RIGHT SURVIVES TO HAVE THOSE DIVIDENDS DECLARED SUBSEQUENTLY, AND THE DIRECTORS THEREAFTER HAVE NO DISCRETION WHATEVER TO DECLARE THOSE DIVIDENDS

The law of the state of incorporation—here the law of Maine—governs in the determination of dividend rights. And the law of Maine, as we shall show, is in full accord with the applicable general rules dealt with recently by this Court in *Guttmann* v. *Illinois Central R. Co.*, 189 F. 2d 927 (1951), cert. den. 342 U. S. 867 (1952), and by the Supreme Court in *Wabash Ry. Co.* v. *Barclay*, 280 U. S. 197 (1930).

A

There is no claim here, as the District Court noted, that the directors who acted in 1940 and earlier years abused their discretion in omitting payment of preferred dividends.

The declaration of those dividends was a matter within the directors' discretion. Maine follows the general rule concerning the power of directors in this respect.

> "As a general rule, the officers of a corporation are the sole judges as to the propriety of declaring dividends, and the courts will not interfere with a proper exercise of their discretion. The company usually establishes its financial policy for itself."
>
> *Belfast & Mooschead Lake R. Co.* v. *Belfast*, 77 Me. 445, 454, 1 Atl. 362, 366 (1885).

> "The officers of a corporation are invested with a discretionary power with regard to the time and manner of distributing its profits. They may use the profits for the development of the company's business, so long as they do not abuse their discretionary power, or violate the charter, or the contracts made, as to profits, with particular classes of stockholders."
>
> *Spear* v. *Rockport-Rockland Lime Co.*, 113 Me. 285, 288, 93 Atl. 754, 756 (1915).

> "The defendants contend that, in the absence of fraud, bad faith or abuse of discretion, their judgment not to pay dividends is conclusive unless their discretion is limited by statute, charter or by-law. With this general principle we concur."
>
> *New England Trust Co.* v. *Penobscot Chemical Fibre Co.*, 142 Me. 286, 290, 50 A. 2d 188, 190 (1946).

In each of these cases, it is true, the Maine court found that an exception to the rule was involved: The directors' discretion does not control where it is limited by the dividend contract set forth in the charter or by-laws. And as the Maine court itself remarked in the *New England Trust* case (*supra*), "Our court has gone further than have

some others in holding that the discretion of directors is limited when the preferred stock contract, as was the case here provides without qualification that stockholders are entitled to dividends at a fixed rate" (142 Me. at 290, 50 A. 2d at 190). Thus, the charter language in the *Belfast & Moosehead Lake* case:— "dividends on the preferred stock *shall* first be made ***" (italics added)—was held to make dividend payment out of earnings mandatory. This was a case of non-cumulative preferred stock. The same result was reached in *Spear* and in *New England Trust* where similar language appeared in the charters, and dividend payment was held mandatory in these two cases which concerned cumulative preferred stock. In the instant case, however, defendant's charter calls for dividends "when and as determined and declared by the Board of Directors". It is clear from the above decisions that such charter language places the case well within the general rule and that the directors were vested with full discretion to determine not to pay dividends in the various years (1940 and earlier) when they were omitted.

B

Maine also follows the general rule concerning the dividend rights of non-cumulative preferred stockholders. The rule is stated by Mr. Justice Holmes in *Wabash Ry. Co.* v. *Barclay,* 280 U. S. 197 (1930); the following excerpt from his opinion, we believe, bears repetition:

> "We believe that it has been the common understanding of lawyers and business men that in the case of non-cumulative stock entitled only to a dividend if declared out of annual profits, if those profits are justifiably applied by the directors to capital im-

> provements and no dividend is declared within the year, the claim for that year is gone and cannot be asserted at a later date" (p. 203).

This statement of "common understanding" is fully confirmed by Professor A. A. Berle, the principal advocate of greater rights for non-cumulative preferred stockholders, as this Court noted in its opinion in *Guttman* v. *Illinois Central R. Co.*, 189 F. 2d 927 (1951), cert. den. 342 U. S. 867 (1952):

> "Berle, a most brilliant legal commentator on corporate finance, who may be credited with the authorship of plaintiff's basic contention, admitted that 'popular interpretation,' including that of 'investors and businessmen,' holds 'non-cumulative' to mean 'that dividends on non-cumulative preferred stock, once passed or omitted, are "dead"; can never be made up.' See Berle, Non-Cumulative Preferred Stock, 23 Columbia Law Review (1923) 358, 364-5." (189 F. 2d, at 930n)

An attempt to find loopholes in the *Wabash* decision was rejected by this Court in the *Guttmann* case. The following states the Court's conclusions:

> "In sum, we hold that, since the directors did not 'abuse' their discretion in withholding dividends on the non-cumulative preferred for any past years, (a) no right survived to have those dividends declared, and (b) the directors had no discretion whatever to declare those dividends subsequently." (189 F. 2d, at 931)

The Maine court has been called upon to consider the point in two cases dealing with a single charter. *Belfast &*

Moosehead Lake R. Co. v. *Belfast*, 77 Me. 445, 1 Atl. 362 (1885), and *Hazeltine* v. *Belfast & Moosehead Lake R. Co.*, 79 Me. 411, 10 Atl. 328 (1887). These are the only cases in Maine that have been found which deal with non-cumulative preferred stock. The following statements by the Maine Supreme Judicial Court in these two opinions are directly to the point here:

> "It was not intended in the present instance to guarantee a dividend. If a dividend is prevented in any one year by a deficit of earnings, it cannot be made up from the earnings of succeeding years." (77 Me. at 452, 1 Atl. at 365)
>
> "Another thing, before spoken of, which favors the complainants is that by our former opinion their dividends are held to be non-cumulative, and if lost now are forever lost." (79 Me. at 420, 10 Atl. at 331-2)

The actual holdings in these two cases, it is true, rest on the finding that the railroad's by-law made the dividend mandatory to the extent of the annual earnings. But the statements quoted above, nevertheless, are not mere obiter; they constituted an important step in the court's reasoning. But even if the above expressions of the Maine court are not to be deemed controlling utterances, then the situation does not differ from that presented in the *Guttmann* case where there were "no Illinois decisions or statutory provisions which control or guide us" (189 F. 2d at 928). In Maine, at the least, we do have guidance, and these expressions as to the local law are completely in conformity with the conclusions reached in *Wabash Ry. Co.* v. *Barclay* and in *Guttmann* v. *Illinois Central R. Co.*

Plaintiff, seeking escape from this situation, has presented the affidavit of a member of the Maine bar (P136). His Maine attorney states that he has examined defendant's charter and has studied the Maine constitution, statutes and cases relating to corporations. But he omits to identify the cases, statutes or constitutional provisions which he considers pertinent here. All that we have from him is a statement of bare conclusions: that the preferred stockholders are entitled to dividends for any year in which there were net profits or surplus, and that "the directors cannot indefinitely postpone payment of preferred dividends" in view of a charter provision (not identified) "which evidences the intention of the parties that the preferred stockholders were to receive yearly dividends if there was a surplus or net profits" (P136-7). The affidavit as submitted to the District Court failed to indicate the reasoning which lay behind these conclusions, nor did it mention the authorities relied on. An effort to remedy this was apparently made thereafter. A list of five Maine cases was added to the affidavit upon the filing of the record on appeal. This improper addition has been stricken (see order of this Court herein dated September 18, 1952), but the five Maine cases will probably be brought to the Court's attention by appropriate means. Two of these cases are the *Belfast & Moosehead Lake* cases already discussed which do deal with non-cumulative preferred stock and which give no support to plaintiff's conclusion. Two more are the *Spear* case and the *New England Trust* case (both *supra*) which are concerned only with cumulative preferred stock. The fifth is *Trask* v. *Chase,* 107 Me. 137, 77 Atl. 698 (1910), in which no preferred stock at all was concerned. The net result is that we have an affidavit from

a Maine lawyer retained by plaintiff who adds nothing to the case but his statement that plaintiff should prevail.

The affidavit of plaintiff's Maine attorney was evidently submitted in an effort to create an apparent issue of fact on the record, and plaintiff now argues (brief, p. 14) that it accomplished this. For such a purpose, however, the affidavit will not serve. Even if it contained a full discussion of Maine authorities, it would present no issue for trial. Maine law is to be established here in the same way that the law of any of the States is found by a federal court. The federal judge takes judicial notice of the laws of all States. Testimony and affidavits are not admissible. The rule is well summed up in *Strickland* v. *Humble Oil & Ref. Co.,* 140 F. 2d 83, 86 (CA 5, 1944), cert. den. 323 U. S. 712 (1944), as follows:

> "The law of a foreign State or country may be proved as a fact by a witness familiar with it. But in a court of the United States no State of the Union is a foreign State. The judge judicially notices the law of them all, and may inform himself in such manner as he chooses [citations omitted]. It is not proper to prove such a matter to the jury by witnesses [citation omitted]."

The rule is long established. *Owings* v. *Hull,* 9 Pet. 607, 625 (1835); *Lamar* v. *Micou,* 114 U. S. 218, 223 (1885); cf. *Hanley* v. *Donoghue,* 116 U. S. 1, 6 (1885). See, also, *In re Paramount Publix Corp.,* 85 F. 2d 83, 86 (CA 2, 1936); 3 Beale, Conflict of Laws, p. 1687. It is a rule of evidence, and is unaffected by the doctrine of *Erie R. Co.* v. *Tompkins,* 304 U. S. 64 (1938),—a point now fully established. *Newman* v. *Clayton F. Summy Co.,* 133 F. 2d 465, 467n (CA 2, 1942); *Gallup* v. *Caldwell,* 120 F. 2d 90, 93-4

(CA 3, 1941); *Strickland* v. *Humble Oil & Ref. Co., supra; Wm. J. Lemp Brewing Co.* v. *Ems Brewing Co.,* 164 F. 2d 290, 293 (CA 7, 1947), cert. den. 333 U. S. 863 (1948). Plaintiff refers (brief, p. 14) to a District Court decision to the contrary (*Affiliated Enterprises, Inc.* v. *Courter Amusement Co.,* 32 F. Supp. 11, EDNY 1940). The case must be regarded as erroneous (see *Newman* v. *Clayton F. Summy Co., supra*). The holdings above leave no room for further dispute on the point.

III

NO GENUINE ISSUE OF FACT IS PRESENTED FOR TRIAL; SUMMARY JUDGMENT WAS PROPERLY GRANTED

The decision below was rendered with full regard for the views which this Court has expressed concerning the granting of summary judgments. Judge Galston concluded his opinion with the following statement:

> "In reaching this decision I have well in mind the admonition of Judge Learned Hand in Bozant v. Bank of New York, 2 Cir., 156 F. 2nd 787. The conclusion reached here is in no sense based on an 'effort to save time by an attempt to dispose of a complicated state of facts on motion for summary judgment'. Whatever there is in the way of complicated statements of facts has no bearing on the pivotal issue raised by the pleadings in this case." (P194a; 101 F. Supp. at 261).

Appellant opens his brief (p. 3) with an acknowledgement that the District Court decision rests solely on a determination of a question of law. But later in his brief he attempts to suggest that there are issues of fact to be tried.

He says (brief, p. 8) that, "Further investigation and cross-examination will undoubtedly reveal the intent of the framers of the instrument [the corporate charter]." And he asserts that a question of fact with respect to Maine law has been raised (brief, p. 14). The matter of Maine law we have dealt with above (*supra*, pp. 26-7). The suggestion that evidence will be adduced to show the intent of the framers of the corporate charter is a similar futile effort to escape from the decision below. It would be strange law that would permit evidence of the mental workings of the original draftsmen to overcome the plain terms of the document executed and in force for over forty years and relied upon by countless holders of both preferred and common stock during those years.

But even so, plaintiff's casual statement that unspecified evidence "will undoubtedly reveal" the intent of the framers —presumably an intent that coincides with plaintiff's position here—will not serve to prevent summary judgment. While this Court has closely confined the field available for summary judgment, it obviously has not abolished that procedure. Thus, in *Engl* v. *Aetna Life Ins. Co.*, 139 F. 2d 469, 473 (1943), where a summary judgment granted below was affirmed, this Court said (*per* Clark, J.) that——

> "* * * we have often held that mere formal denials or general allegations which do not show the facts in detail and with precision are insufficient to prevent the award of summary judgment."

And in *Radio City Music Hall Corp.* v. *United States*, 135 F. 2d 715, 718 (1943), a summary judgment granted upon affidavits and depositions was also affirmed by this Court even though the opposing party there was "forced to draw all its evidence from the plaintiff's own officers". The fol-

lowing excerpt from Judge Learned Hand's opinion is directly to the point:

> "When a party presents evidence on which, taken by itself, it would be entitled to a directed verdict if believed, and which the opposite party does not discredit as dishonest, it rests upon that party at least to specify some opposing evidence which it can adduce and which will change the result."

Again, in *Arnstein* v. *Porter,* 154 F. 2d 464 (1946), where a summary judgment was reversed, the Court (*per* Frank, *J.*) stated this test: "that at the close of a trial the judge could properly direct a verdict" (p. 470).

In *Associated Press* v. *United States,* 326 U. S. 1 (1945), a summary judgment in a most complex case was affirmed, the Supreme Court noting that "the court below * * * carefully abstained from the consideration of any evidence which might possibly be in dispute" (p. 6).

It is thus well established that within its proper limits summary judgment is an appropriate procedure; that it may not be avoided merely by the bald assertion that there is an issue of fact; nor is it to be denied where the material facts are undisputed merely because the opposing party would like to litigate collateral issues which are not essential to decision. The case here rests squarely upon the terms of the preferred stock contract set forth in the charter. There is no genuine issue of fact. After trial in which the motives and intentions of the present directors would be explored at length, the case must still be determined upon the rights created by the terms of the charter and that determination, as in the *Guttmann* case, must be in favor of defendant. This is eminently a case for summary judgment.

The decision below, we submit, was correct and should be affirmed. It was made by a Judge who thoroughly and conscientiously examined the record, and who was completely familiar with the law relating to non-cumulative dividends, having previously decided the *Guttmann* case in the lower Court. The judgment below may well be affirmed on his opinion.

Respectfully submitted,

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